STATE OF CALIFORNIA ARNOLD SCHWARZENEGGER, *Governor*

PUBLIC UTILITIES COMMISSION
505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298

December 9, 2003 **Agenda ID #3078**
Ratesetting

TO: PARTIES OF RECORD IN RULEMAKING 02-01-011

This is the draft decision of Administrative Law Judge Pulsifer. It will not appear on the Commission's agenda for at least 30 days after the date it is mailed. The Commission may act then, or it may postpone action until later.

When the Commission acts on the draft decision, it may adopt all or part of it as written, amend or modify it, or set it aside and prepare its own decision. Only when the Commission acts does the decision become binding on the parties.

Parties to the proceeding may file comments on the draft decision as provided in Article 19 of the Commission's "Rules of Practice and Procedure." These rules are accessible on the Commission's website at http://www.cpuc.ca.gov. Pursuant to Rule 77.3 opening comments shall not exceed 15 pages. Finally, comments must be served separately on the ALJ and the assigned Commissioner, and for that purpose I suggest hand delivery, overnight mail, or other expeditious method of service.

/s/ Angela K. Minkin
Angela K. Minkin, Chief
Administrative Law Judge

ANG: avs

Decision **DRAFT DECISION OF ALJ PULSIFER (Mailed 12/9/2003)**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking Regarding the Implementation of the Suspension of Direct Access Pursuant to Assembly Bill 1X and Decision 01-09-060.	Rulemaking 02-01-011 (Filed January 9, 2002)

OPINION ADOPTING SHORT-TERM PRICE PROXY

I. Introduction

By this decision, we adopt a proxy for pricing of short-term power procured to serve Direct Access (DA) customers returning to bundled service on a temporary basis. Decision (D.) 03-05-034 required that DA customers returning on a temporary bundled service (TBS) basis must "pay for the incremental cost that will be imposed on the system due to additional short-term spot supplies procured to serve them" (pg. 19). The Commission further ordered that the remaining bundled customers should not be burdened with these added costs and that these customers should be left indifferent to whether DA customers use the utility as temporary "safe harbor." (D.03-05-034, pp. 19 – 20.) As explained below, we adopt the California Independent System Operator (CAISO) 10-minute Ex Post Incremental (INC) price as the applicable proxy.

II. Background

D.03-06-035 granted limited rehearing on the issue of a suitable proxy for the short-term commodity cost of electricity.[1] This cost would be borne by those DA customers who require bundled service as a temporary "safe harbor" before moving to a new Energy Service Provider. D.03-06-035 directed that this matter be addressed through a Rule 22 Working Group Meeting, (p.13) which was held on August 29, 2003. Participants in the workshop included Pacific Gas and Electric Company (PG&E), Southern California Edison Company (SCE), San Diego Gas & Electric Company (SDG&E), The Alliance of Retail Energy Markets/Western Power Trading Forum (AReM/WPTF), The California Manufacturers & Technology Association (CMTA) and Energy Management Services (EMS).

At the Working Group Meeting, five separate proposals were initially presented regarding the appropriate short-term proxy price, four of which were similar.[2] Through discussions, those parties offering similar proposals were able to agree on a single proposal based on the California Independent System Operator (ISO) real-time INC price. The INC price represents the market clearing price set by the marginal resource generating the energy purchased by the ISO to cover imbalance energy, *i.e.*, the difference between scheduled energy and energy required to support real-time load. Metered load in excess of scheduled load is charged the INC price.

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[1] In addition to the electric commodity costs, safe harbor, Direct Access load is expected to also pay additional costs such as the California Independent System Operator's grid management costs, ancillary service costs, UFE, transmission and distribution losses, and franchise fees and uncollectibles.

[2] The four similar proposals were offered by SDG&E, SCE, AReM/WPTF and CMTA.

On September 15, 2003, parties submitted a "Status Report" summarizing these discussions and the proposals submitted. Participants did not reach full agreement on a price proxy proposal as a result of the workshop, but did agree on the advisability of participants filing an additional brief in support of their respective proposals for the Commission's consideration. By Administrative Law Judge ruling dated September 25, 2003, parties were granted leave to file briefs regarding their positions on price proxies. Briefs were filed on October 10, 2003.

III. Position of Parties

A. Position of PG&E

PG&E was the only party to disagree with the use of the INC price as a proxy for TBS customers. PG&E instead offered a second proposal calling for the TBS price proxy to be based on the day-ahead short-term price indices published by the Intercontinental Exchange (ICE). The ICE 10x Day Ahead Power Price Report publishes short-term indices that represent prices paid for actual day-ahead transactions for standard products.

PG&E proposes that ICE indices be adopted for purposes of setting a TBS short-term power price for the commodity cost of power to be determined as follows. For PG&E, for on peak hours (as defined by ICE) the day ahead North-of-Path 15 weighted average (by transaction volume) index. For off peak hours, the day ahead North-Of-Path 15 off peak weighted average index. For SCE and for SDG&E, the analogous South-Of-Path 15 indices would be used.

PG&E claims that ICE indices provide a more accurate proxy than the ISO INC price for the markets in which the utilities are likely to procure power for anticipated load, including TBS load in the utility's day-ahead procurement process. PG&E claims there is no basis for believing that, as a general matter, TBS load is served by the ISO INC market. PG&E notes that broker prices, such as those provided by ICE, have been acknowledged by the Commission for use by the utilities in procurement.[3] All three utilities have used ICE as a vehicle to facilitate day-ahead transactions.[4]

PG&E opposes the use of the ISO INC index for purposes of TBS pricing. PG&E argues that because the ISO INC market is where utilities' *unanticipated* energy needs are met, ISO INC prices do not reflect the cost to serve TBS loads that *are anticipated* by the utility in advance. As such, PG&E argues that TBS pricing should be incorporated into the utility's day ahead procurement process. Therefore, as indicated in Figure 2 on page 7 of the Status Report, the ISO INC price has not tracked loads at certain times, but instead has gone down as loads go up. This also suggests that ISO INC prices may not serve as a reasonable proxy for the price actually paid.

PG&E argues that both the ICE indices and ISO INC prices are transparent and verifiable. As the Status Report indicates, day-ahead ICE prices can be viewed free of charge on their website.[5] Published information includes delivery location, highest price, lowest price, weighted average price, change in price from previous trading session, volume in MWh, number of trades executed, and number of companies executing trades. Therefore, PG&E argues, the ICE price is easily accessible, and there is no basis for favoring the ISO INC price over the ICE indices on accessibility grounds.

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[3] *See*, D.02-10-062, pp. 30-32.

[4] Status Report, p. 5.

[5] Status Report, p. 5.

B. Position of Joints Parties

The Joint Parties (*i.e.*, all workshop participants other than PG&E) support use of the CAISO real-time INC price for TBS pricing purposes. Joint Parties contend that the INC price is the only transparent, verifiable market-clearing price index available in California. Thus, after the demise of the PX, the INC price is the best indicator of short-term market clearing prices. To the extent that the ISO implements day-ahead and/or hour-ahead energy markets as part of its pending market redesign, the INC price can be replaced by these new price indices if and when the Commission deems appropriate.

Since the utilities propose to calculate the safe harbor tariff rate in the same way as the former Schedule PX, the Joint Parties argue, the volatility and occasional spiking of real-time INC prices, especially in summer peak periods, will not harm safe harbor customers. By contrast, the graph on page 3 of the Status Report shows that in almost 70% of the hours, the ICE prices were significantly higher than the average INC prices for the same period based on a comparison of SP-15 hourly average INC prices to on-peak and off-peak ICE SP-15 day ahead prices (as proposed by PG&E) for the month of August 2003. As noted in the Status Report, the monthly unweighted daily average of ICE prices was more than $9.00 per MWH higher than unweighted hourly average of INC prices.

Joint Parties further argue that the California ISO real-time market is more well-known to DA customers than any other power spot market in California after the demise of the PX, and thus, use of a non-ISO market index would require more education of customers than would use of an ISO-based price.[6]

Joint Parties argue that use of the INC price will ensure that other bundled customers are not adversely affected by the return of DA customers to bundled service. It will also free the utilities of the burden of forecasting and procuring supplies to meet the load requirements of returning DA customers, and will eliminate the risk to the utility and other ratepayers of incurring new stranded costs to meet that load.

Joint Parties argue that using the INC price mirrors the approach being taken by an increasing number of other states for pricing default utility service that do not have the option of relying on traditional bundled utility service on a long-term basis. Specifically, “default” or “standard offer” service for such customers is increasingly based on the ISO’s hourly market-clearing price, plus an adder to compensate for the utilities' administrative/brokerage costs to provide the default service.

IV. Discussion

We conclude that while both of the alternative proxies proposed by parties represent short-term market prices, the CAISO INC price is the more appropriate proxy, and we hereby adopt it for TBS purposes. SDG&E, in its comments, identifies three criteria to consider in evaluating a price proxy: (1) relationship of the proxy price to the actual costs of utility service; (2) price transparency; and (3) dependability and continuity of the source of the price. We are persuaded,

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[6] The Status Report also notes at page 3 that, “The hourly Integrated Forward Market (IFM) which the ISO is developing may provide a superior proxy price for TBS than the real-time INC price. The proxy price issue should be revisited when the IFM is underway.” The Joint Parties concur with this recommendation.

and thus, by these comments, conclude that these criteria reasonably define a conceptual framework for selection of a suitable price proxy. We also conclude that the INC proxy meets these criteria better than does the ICE index. We thus decline to adopt the ICE as a proxy, as proposed by PG&E.

Since the ISO pays the INC price to generators to increase output when generation is not sufficient to meet load, this proxy represents a current marginal price that is appropriate to charge to safe harbor customers. Although the utilities will be buying imbalance energy from the ISO and paying INC prices for it, the utilities will not all necessarily be buying energy through the ICE or any other particular exchange and paying their particular index prices for it. Thus, a proxy from a market used continually by all three utilities is more appropriate than a proxy from one particular private exchange. The INC price provides a uniform price that can be applied on a statewide basis, thereby avoiding the situation where returning DA customers pay differing prices, depending upon the service territory location of their facilities.

The Status Report also addresses several undisputed "technical adjustments" regarding how to calculate the final price to be charged TBS customers.[7] The three utilities agree to clarify their tariff filings to explicitly state that the ISO Grid Management Charge (GMC) for Congestion (Charge Type 522 Interzonal Scheduling GMC) should not be included in the TBS rate. The three utilities also agree to explicitly state the billing determinant for the GMC components included in the TBS rate.

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[7] Status Report, p. 8.

The three utilities agree that the UFE modifier be based on recent historical numbers available from the ISO, and that it should be adjusted no more than semi-annually if actual UFE departs from the historical rate.

V. Comments on Draft Decision

The Draft Decision of Administrative Law Judge Thomas R. Pulsifer in this matter was mailed to the parties in accordance with Section 311(g)(1) of the Pub. Util. Code and Rule 77.7 of the Rules of Practice and Procedure. Comments were filed on _____________, and reply comments were filed on _____________.

VI. Assignment of Proceeding

Carl W. Wood and Geoffrey F. Brown are the Assigned Commissioners and Thomas Pulsifer is the assigned Administrative Law Judge in this proceeding.

Findings of Fact

1. Decision 03-05-034 required that DA customers returning on a TBS basis must "pay for the incremental cost that will be imposed on the system due to additional short-term spot supplies procured to serve them."

2. In selecting a TBS price proxy, the following criteria reasonably define a suitable conceptual framework: 1) relationship of the proxy price to the actual costs of utility service; 2) price transparency; and 3) dependability and continuity of the source of the price.

3. The INC price better meets the criteria for a suitable TBS proxy than does the ICE index.

4. The use of the INC price will ensure that other bundled customers are not adversely affected by the return of DA customers to bundled service.

5. The Status Report also addresses several undisputed "technical adjustments" regarding how to calculate the final price to be charged TBS customers.

6. The three utilities agree to clarify their tariff filings to explicitly state that the ISO Grid Management Charge (GMC) for Congestion (Charge Type 522 Interzonal Scheduling GMC) should not be included in the TBS rate.

7. The three utilities also agree to explicitly state the billing determinant for the GMC components included in the TBS rate.

8. The three utilities agree that the UFE modifier should be based on recent historical numbers available from the ISO, and that it should be adjusted no more than semi-annually if actual UFE departs from the historical rate.

Conclusions of Law

1. As directed in D.03-05-034, a price proxy should be adopted for TBS customers that best meets the criteria set forth in Finding of Fact 2 above.

2. The Commission should adopt the INC price as a TBS proxy since it better meets the criteria set forth in Finding of Fact 2 above.

3. The undisputed "technical adjustments" identified in the Status Report are reasonable and should be adopted.

O R D E R

IT IS ORDERED that:

1. The California Independent System Operator 10-minute Ex Post Incremental price is hereby adopted as the applicable proxy for Temporary Bundled Service (TBS) provided to Direct Access customers under the "safe harbor" provisions as set forth in Decision 03-05-034.

2. The investor-owned utilities are hereby authorized to implement this pricing proxy provisions of this order effective immediately.

3. The "technical adjustments" identified in the Status Report, page 8, that are not disputed by any party are hereby adopted. Pursuant to these technical adjustments, three utilities shall clarify their tariff filings to explicitly state that the ISO Grid Management Charge for Congestion (Charge Type 522 Interzonal Scheduling GMC) is not included in the TBS rate. The three utilities shall explicitly state the billing determinant for the GMC components included in the TBS rate. The UFE modifier shall be based on recent historical numbers available from the ISO, and that it should be adjusted no more than semi-annually if actual UFE departs from the historical rate.

This order is effective today.

Dated ____________________, at San Francisco, California.